

Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. As end users of tangible personal property located in Illinois, lessors owe Use Tax on their cost price of such property. See 86 Ill. Adm. Code 130.220. (This is a GIL).

September 18, 2002

Dear Xxxxx:

This letter is in response to your letter dated May 21, 2002. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), which can be found on the Department's website at www.revenue.state.il.us/Laws/regs/part1200/.

In your letter, you have stated and made inquiry as follows:

Our company is in the lease to own business. We have furniture, electronics and appliances. Much like a Rent-A-Center. When a customer enters into an Agreement with us they have four options:

1. The customer can lease the merchandise and return at anytime they decide that they no longer need it.
2. If the customer does not make their monthly payment the Agreement automatically terminates & the merchandise is returned to our store.
3. The customer can go the full term of the agreement usually anywhere from 12 to 24 months. Make monthly payments for 12 or 24 months depending on how many months the agreement is written up for, and at the end of the term, they become the owners of the merchandise once the last monthly payment is made.
4. They may decide that they want to own the merchandise and pay it off before the term is up. This is called an Early Payout. The customer can do this at anytime.

We pay use tax in the amount of 6 1/4% to the State of Illinois for every piece of merchandise that is shipped to us.

Our question is this. **Since we never know if the customer is going to want to own the merchandise**, if a customer decides to do an Early Payout, do we collect Sales Tax at 7 3/4% (in our area) on the unpaid balance due up to that point? Example - A customer enters into a Lease To Own Agreement with us. The Cash price is \$1111.99. The customer makes two monthly payments **to lease** the merchandise for a total

amount of \$305.76. His unpaid balance now is \$806.23. Do we collect Sales Tax on the \$806.23?

I am enclosing a copy of our Agreement for your review. Can your department please send us a Private Letter Ruling and mail it.

Thank You.

Please note that the State of Illinois taxes leases differently for Retailers' Occupation Tax and Use Tax purposes than the majority of other states. For Illinois sales tax purposes, there are two types of leasing situations: conditional sales and true leases. A conditional sale is usually characterized by a nominal or one dollar purchase option at the close of the lease term. Stated otherwise, if lessors are guaranteed at the time of the lease that the leased property will be sold, this transaction is considered to be a conditional sale at the outset of the transaction, thus making all receipts subject to Retailers' Occupation Tax.

A true lease generally has no buy out provision at the close of the lease. If a buy out provision does exist, it must be a fair market value buy out option in order to maintain the character of the true lease. Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See the enclosed copy of 86 Ill. Adm. Code 130.220. As end users of tangible personal property located in Illinois, lessors owe Use Tax on their cost price of such property. The State of Illinois imposes no tax on rental receipts. Consequently, lessees incur no tax liability.

The above guidelines are applicable to all true leases of tangible personal property in Illinois except for automobiles leased under terms of one year or less, which are subject to the Automobile Renting Occupation and Use Tax found at 35 ILCS 155/1 et seq.

As stated above, in the case of a true lease, the lessors of the property being used in Illinois would be the parties with Use Tax obligations. The lessors would either pay their suppliers, if their suppliers were registered to collect Use Tax, or would self-assess and remit the tax to the Department. If the lessors already paid taxes in another state with respect to the acquisition of the tangible personal property, they would be exempt from Use Tax to the extent of the amount of such tax properly due and paid in such other state. See 86 Ill. Adm. Code 150.310(a)(3) enclosed.

Persons who are lessors and whose only selling activity consists of selling items that come off lease and are no longer needed for rental purposes cannot purchase for resale. If an item is placed in a rental inventory, it has been purchased for rental purposes and Use Tax is due. "Rental inventory" means that the owner, in order to state his intended use of the property as rental property, has recorded the property in his books and records as rental property in accordance with generally accepted accounting principles. Depreciation of property used for rental purposes demonstrates an intent to include that property in rental inventory. See 86 Ill. Adm. Code 130.2013.

The question of whether a lessor's sale of tangible personal property coming off lease that is no longer needed for the lessor's rental inventory is subject to Retailers' Occupation Tax liability depends on whether the seller is strictly a lessor, or whether the seller is otherwise engaged in the business of selling like-kind property. Except in the case of motor vehicles, as explained at 86 Ill. Adm. Code 130.111 (see enclosed copy), a person who is strictly a lessor and whose only sales are of items no longer needed for his rental inventory does not incur Retailers' Occupation Tax liability on those sales.

For example, a lessor of computer equipment who does not maintain a sales inventory of computer equipment and who does not otherwise hold himself out as being in the business of selling like-kind property, incurs no Retailers' Occupation Tax liability on sales of computer equipment that he no longer wants in his rental inventory. This would be true even though the lessor advertised such sales and was required to make a considerable number of such sales over time. As long as all of the sales are of equipment no longer needed for the lessor's rental inventory, they constitute non-taxable isolated or occasional sales. See 86 Ill. Adm. Code 130.110. However, the rule is different if the lessor is otherwise engaged in the business of selling like-kind property at retail. A lessor of tangible personal property who sells like-kind property apart from his sale of items no longer needed for his rental inventory incurs Retailers' Occupation Tax liability on all retail sales of that property including sales of items no longer needed for his rental inventory. This is true because a person who is engaged in the business of selling tangible personal property cannot make an isolated or occasional sale of like-kind tangible personal property.

A lessor whose only sales are sales of items coming off lease that are no longer needed for his rental inventory incurs no Retailers' Occupation Tax liability on those sales. Lessors who are otherwise engaged in the business of selling like-kind property incur Retailers' Occupation Tax liability on all their sales, including sales of items coming off lease that are no longer needed for their rental inventories.

A lessor who incurs a Retailers' Occupation Tax liability on the sale of an item can take a credit against that liability for any Use Tax and any local Retailers' Occupation Tax reimbursements that he paid to a supplier registered to collect Illinois tax when he purchased that particular item. However, this credit cannot exceed the amount of Retailers' Occupation Tax incurred by the lessor/retailer when he sells the item. Further, only the entity that originally paid the tax on the item can take the credit on the subsequent sale. See 86 Ill. Adm. Code 130.2013. If a lessor filed a return and paid the tax directly to the Department, the lessor must file a claim to recover it.

The agreement you attached to your document does not guarantee a sale of the tangible personal property at the inception of the contract as is common with most conditional sales agreements. Because the lessee appears free to walk away from the lease at any time and therefore a sale of the property is not guaranteed at the time the lease is entered into, our tentative conclusion is that the agreement is a true lease. However, we cannot give a definitive conclusion regarding the nature of the agreement without more detailed information regarding the transactions. Your tax liability for lease items sold is determined by the overall nature of your business as explained in Section 130.2013.

I hope this information is helpful. The Department of Revenue maintains a website, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b).

Very truly yours,

Melanie A. Jarvis
Associate Counsel

MAJ:msk
Enc.